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IN THE

Supreme Court of the United States

OCTOBER TERM, 1950.

No. 472

IN THE MATTER OF
LUSTRON CORPORATION,
BANKRUPT.

LAFAYETTE STEEL CO., INC.,
Petitioner,

vs.

LUSTRON CORPORATION, ET AL.,
Respondents.

REPLY OF PETITIONER TO BRIEF OF RESPONDENTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

AMENDMENT TO PETITION FOR WRIT OF CERTIORARI.

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STATEMENT.

At various points in their answer Respondents allude to the proceeding in the Ohio court begun by RFC as "a general equity insolvency proceeding" (answer, p. 2) or as an "insolvency proceeding" (answer, p. 9). The Ohio proceeding was simply an action to enforce mortgage liens in which the RFC requested and obtained the appointment of a receiver for the mortgaged property and the extension of the receivership to all the debtor's property (R. 38). The Ohio proceeding was in no sense an insolvency proceeding under any insolvency or bankruptcy statute.

ARGUMENT.

Respondents' Answer asserts that the writ of certiorari should not be granted in this cause because the question involved "has been settled by this Court, and the conclusion of the Court of Appeals is based on the prior applicable decisions of this Court" (answer, p. 6). Yet Respondents' own arguments on the merits of the legal issues in this case, to which the major part of their answer is devoted, demonstrate that this case involves important, unsettled issues of a fundamental character which should be settled by a decision of this Court.

1. Thus Respondents endeavor to answer Petitioner's contention that Ohio law applies to determine the title and property rights of Petitioner arising out of the judicial sale in question by urging in this Court for the first time[1] that Ohio law does not apply because the sale is governed by a federal statute, Title 28 U. S. C., § 2004. The question of what law, whether state law or another body of law, governs the effect of a federal equity court sale, and the question of what is the specific rule of law applicable, if state law does not apply, which are implicit in determining what title and interest are acquired before confirmation by a purchaser at the sale, are questions of basic importance in the administration of the Federal judicial system.

Title 28 U. S. C., § 2004 contains but the barest of procedural provisions as to judicial sales of personal property. It provides merely that any personalty sold under any order or decree of any court of the United States shall be sold in accordance with § 2001 unless the Court orders

1. Respondents did not either in the Court of Appeals or in the Bankruptcy Court contend that § 2004 of Title 28, U. S. C. applied. Respondents at the hearing in the Court of Appeals conceded that Ohio law applied.

otherwise. § 2001 provides merely that real estate sold under the order of a federal court shall be sold at public sale held at one of certain located court houses or on the premises, and in addition permits a federal court to order a private sale of real estate on compliance with certain procedural provisions. § 2004 thus contains nothing which either expressly or impliedly determines or affects the title and interest which a purchaser acquires or a debtor loses under a federal court's judicial sale of personal property. Its very narrow procedural provision does not exclude the application of state law in determining this issue.

On the other hand, there are definite indications that, notwithstanding § 2004, state law may well be applicable in determining what is the title and interest a purchaser acquires at a federal court sale. Despite the enactment since 1893 of the Federal Judicial Sales Act (of which § § 2001 and 2004, Title 28 U. S. C., formerly § § 846 and 847, are a part), there has been no weakening or change in the doctrine established by this court in *Brine* v. *Hartford Fire Ins. Co.*, 96 U. S. 627, 635 (1878), sixty years before *Erie Ry. Co.* v. *Tompkins*, 304 U. S. 64 (1938), that in order to avoid introducing into the jurisprudence of a state "the discordant elements of a substantial right which is protected in one set of courts and denied in the other with no superior to decide which is right" the effect of a federal court judicial sale on the rights acquired by the purchaser is subject to state rules of property. *American Mine Equipment Co.* v. *Ill. Coal Corp.*, (C. A. 7) 31 F. (2d) 507; *O'Connor* v. *Townsend*, (C. A. 8) 87 F. (2d) 882. Of course, this doctrine has had even greater vitality since this court's decision in *Erie Ry. Co.* v. *Tompkins, supra.*

The policy considerations stressed in *Erie Ry. Co.* v. *Tompkins* are especially involved here. The rule of law in many states is that the purchaser of property at a judicial sale is the equitable owner of the property even before the

sale is confirmed, although his title may be defeated if confirmation should properly be denied.[2] If Respondents' contentions as to § 2004 of the Judicial Code are sustained, then on exactly the same facts involving a judicial sale of property in a state following such rule, where the sale had not been confirmed when bankruptcy intervened, there will be diametrically opposite results as to the debtor's rights to the property, depending on whether it was a federal court or a state court which ordered the sale. Thus, if the sale were ordered by a federal court, the debtor's trustee in bankruptcy would be entitled to the property; whereas if the sale were ordered by a state court, the purchaser at the sale, subject to confirmation, would be entitled to the property. This Court should decide whether anything in § 2004 requires such an untoward result.

Moreover, even if it be assumed that the existence of § 2004 of the Judicial Code necessarily excludes the application of state law in determining what is the title and interest a purchaser acquires before confirmation at a federal court judicial sale, it does not follow that the specific rule of law to govern is the one adopted by the Court of Appeals in this case. The authorities on this question are irreconcilably divided. There are federal cases, principally on sales under the specific sales provisions of the Bankruptcy Act, which support the decision of the court below. But as shown in the Petition (p. 9), there are also a very substantial number of state and federal decisions to the contrary, which hold that a purchaser at a judicial sale acquires an equitable title immediately at the sale, although the sale is not complete until confirmed and the purchaser may lose his title should the sale not be confirmed. There is no decision of this court which is decisive of the question. In view of the importance of the question in the operation of the bankruptcy act and in the administration of the

2. Many of the authorities are referred to in footnote 13, p. 9 of the Petition in this case.

federal judicial system, this court should resolve the conflict in the authorities and decide which rule shall be followed by the federal courts.

2. Respondents' claim (answer, pp. 10-15) that the Ohio rule as to the title and rights acquired before confirmation by a purchaser at a judicial sale is the same as the rule expressed in the federal cases cited by the court below, which for the greater part involve sales under the sales section of the bankruptcy act. The Ohio authorities cited by Respondents in the main are the same as those cited in the opinion of the Court of Appeals in this case. As was pointed out in the Petition in this case, (p. 10) none of the Ohio cases cited by the Court of Appeals dealt specifically with the title or rights acquired before confirmation by a purchaser at a judicial sale and the *obiter dicta* in those cases, to the effect that the sale is not complete until confirmed or that the purchaser loses his rights if confirmation should be denied, are in no way inconsistent with the principle that the purchaser at such a sale acquires an equitable title before confirmation. There is not a single Ohio case, and certainly Respondents cite none, which states even by way of *dictum* that the Ohio law is what Respondents claim: that prior to confirmation the purchaser is merely "a preferred proposer and not the purchaser."[3]

3. The only authority Respondents cite to support this contention is 24 Ohio Jurisprudence, Judicial Sales, § 105, p. 79. This encyclopedia does not cite a single Ohio decision in support of this proposition, but cites only another encyclopedia published by the same publisher, 16 Ruling Case Law, p. 114, § 82. Ruling Case Law, also, fails to cite a single Ohio decision to support its statement of this proposition. However Ruling Case Law qualifies its statement of the proposition to show that the generally accepted law is to the contrary of what Respondents urge and that even before confirmation of a judicial sale "the highest bidder to whom the property has been struck off and who has paid his deposit in good faith acquires an equitable and inchoate title; and this is a vested and definite legal right which is recognized and enforced by law, and must be respected by the court * * *"

In cases involving the risk of loss where property is lost or damaged, the risk of loss is placed on the "owner." In such cases where the property is lost or damaged after a judicial sale is held but before the sale is confirmed, it makes a real difference whether the purchaser is the equitable owner of the property or is merely a "preferred proposer" without any title or rights to the property. These cases really test whether the rule of law is the one way or the other. In such a case, the federal decisions involving sales under the bankruptcy act sales provision upon which the Court below relied and which Respondents claim do not differ from the Ohio law, place the risk of loss not on the purchaser but on the receiver or trustee conducting the sale, *Hartford Accident & Indemnity Co.* v. *Crow,* (C. A. 6) 83 F. (2d) 386, 387. The Ohio decisions, however, indicate that the risk of loss is on the purchaser. *Murphy* v. *Hardee,* 22 Oh. C. C. 511, 517; *Schmidt* v. *Penn Mutual Life Ins. Co.,* 25 Oh. L. A. 652, 655. These Ohio cases demonstrate that regardless of what language or *dictum* may be found in the Ohio decisions, in situations where it really makes a difference, the Ohio courts regard a purchaser at a judicial sale as the equitable owner of the property purchased even before the sale is confirmed. *Johnson* v. *Cincinnati,* 11 Oh. C. C. (N. S.) 344, 346, an Ohio Circuit Court case from which Respondents quote (answer, p. 14), if it stands for anything, demonstrates that where it is necessary to protect the purchaser at a judicial sale the Ohio courts will consider him as the equitable owner before confirmation although they may not do so where the protection of his rights is not involved.

Respondents assert *Oviatt* v. *Brown,* 14 Oh. 285 and *Boyd* v. *Longworth,* 11 Oh. 235, cited in the Petition (p. 9) are inapplicable because they "involve a sheriff's sale which by the Ohio statute relating to sheriff's sales vested title in the purchaser at the date of sale" whereas the instant

case involves "a judicial sale by a receiver * * * subject to confirmation." It is true that these cases involve sheriff's sales. But Respondents overlook what those cases show plainly: (1) the sheriff's sales in those cases, like judicial sales, were subject to confirmation by the court which entered the judgment; and (2) under the statute governing the sheriff's sales, full title was not vested in the purchaser "at the date of sale" but the sheriff's deed when executed after confirmation, like the deed in connection with a judicial sale, vested in the purchaser "the title from the date of the sale. The deed executed at a subsequent date has relation back to that date and is as effectual as if then made." *Oviatt* v. *Brown,* 14 Oh. 285, 294.[4] The decisions of the Ohio Supreme Court in *Oviatt* v. *Brown* and *Boyd* v. *Longworth,* are thus equally as applicable to judicial sales as to sheriff's sales, and establish the title and property interest which a purchaser at a judicial sale acquires under Ohio law before the sale is confirmed.

Respondents rely strongly on *Hoyd* v. *Citizens Bank of Albany Co.* (C. A. 6) 89 F. (2d) 105, 108 as supporting their contention as to the Ohio rule. In that case an agricultural composition or extension proceeding under §§ 75 (a) to (n) of the Bankruptcy Act had been filed after the real estate of the debtor, located in Ohio, had been sold under an Ohio State court's decree of foreclosure. The sale had not been confirmed when the bankruptcy proceeding was filed. The court there held that the debtor's statutory right under § 11690, General Code of Ohio, to redeem from the foreclosure sale at any time before its confirmation "constituted property which was subject to the jurisdiction of the federal court under § 75(n)". This decision

4. Compare *Jashenosky* v. *Volrath,* 59 Oh. St. 540, 545, which enunciates the same rule of relation back with respect to deeds executed under judicial sales.

was based entirely upon the debtor's statutory right to redeem from a sale of real estate, granted by the Ohio statute, and not, as Respondents claim, upon any hypothesis that under Ohio law a purchaser of property at a judicial sale has no title or rights as to the property before the sale is confirmed. The Ohio statute expressly limits the right of redemption to sales of "real estate" and there is, under Ohio law, no right of redemption from a judicial sale of personal property,[5] which is all that the instant case involves. The *Hoyd* case is thus inapplicable and gives no support to Respondents' contention.

In all, Respondents have failed to discredit or weaken the pronouncement of the Supreme Court of Ohio in *Parker* v. *Storts*, 15 Oh. St. 351, 354, referred to in the Petition, that a purchaser at a judicial sale where, as in the instant case, "the proceedings are legal and regular, and no ground exists for setting aside the sale, becomes, by his purchase, and by the payment of the purchase money or compliance with the terms of sale, the equitable owner of the premises; and though he may not be invested with the legal title till the confirmation of the sale, and the execution of a conveyance by the proper officer; yet, when the legal title is thus vested, for many purposes it relates back to the day of sale." This statement still expresses the Ohio law on this point.

The proper determination of the Ohio law in this case is not a simple matter, but requires substantial familiarity with Ohio law and practice as well as the careful weighing and analysis of the decisions of the Ohio courts. Ohio is outside the circuit of the Court below, and its experience with Ohio law is therefore relatively limited. Its decision denying that Petitioner acquired any title or rights under Ohio law is in direct conflict with the order on the same

5. 24 Ohio Jurisprudence, Judicial Sales, § 141, p. 104.

matter of the United States Court for the Southern District of Ohio, a court which daily passes on matters involving Ohio law, and which recognized and confirmed the title and rights petitioner had acquired at the judicial sale.[6] The instant case is thus of especial importance in implementing the policy of *Erie Ry. Co.* v. *Tompkins,* 304 U. S. 64 and the Rules of Decision Act (28 U. S. C., § 1652) and merits review by this Court.

3. Respondents contend (Answer p. 15) that the argument of petitioner that the appointment of the Ohio receiver was the levy of an equitable execution which imposed a judicial lien upon all assets coming into the Ohio receiver's possession, is not material or relevant, and their answer does not discuss this point. However, regardless of Respondents' present views, the court below based its decision that § 67a(3) of the Bankruptcy Act was not applicable to protect petitioner entirely on its conclusion that "the Ohio receiver's sale was not in pursuance of any lien but a sale of general assets." (R. 325). As pointed out in the Petition (p. 12), this holding is contrary to numerous long standing decisions of almost every Court of Appeals, including the Court below and casts doubt and confusion upon what until now had been established law.

4. Respondents rely strongly, as did the Court of Appeals below, upon the rule of bankruptcy law expressed in *Taylor* v. *Sternberg,* 293 U. S. 470; *Isaacs* v. *Hobbs Tie & Timber Co.,* 282 U. S. 734 and other cases, that upon the

6. The situation presented in this case of a federal court relatively unfamiliar with Ohio law deciding a question of Ohio law contrary to the conclusion in the same matter of a federal court in Ohio, and the submission of a question of Ohio law to this Court for review without the aid of the opinions of lower courts familiar with Ohio law, is a graphic illustration of the serious complications resulting from the denial below of the RFC's motion to transfer the bankruptcy proceedings to the Ohio federal court. Review of the denial of that motion is sought in this court by the RFC in Case No. 507, this term, *RFC* v. *Lustron Corp.*

filing of a petition in bankruptcy, the bankruptcy court acquires paramount and exclusive jurisdiction over all the property of the debtor. Their contention is that since the superior jurisdiction of bankruptcy had intervened before confirmation of the sale to petitioner, the Ohio court lost jurisdiction and had no power to confirm the sale, and therefore petitioner acquired no title or rights to the property purchased.

This contention assumes that without confirmation by the Ohio court, petitioner could have no title of any kind or any right to the property. The assumption is fallacious. By reason of the judicial sale and even before its confirmation, when bankruptcy intervened petitioner had substantial rights and obligations as to the property and under Ohio law was the equitable owner of and had an equitable title to the property. Moreover, Respondents' contention completely disregards § 67a(3) of the Bankruptcy Act. Supposing the paramount and exclusive jurisdiction of the bankruptcy court which Respondents contend attached when the bankruptcy petition was filed against Lustron, nevertheless at that time petitioner already had an equitable title to the property. Whatever that title consisted of, it was expressly declared valid by § 67a(3) of the Bankruptcy Act. Nothing in the rules as the exclusive and paramount jurisdiction of bankruptcy courts takes away from third persons, strangers to the legal proceedings, existing property rights expressly declared valid by a specific provision of the Bankruptcy Act.

Confirmation by the Ohio court, to use apt words of the Ohio Supreme Court, gave petitioner "no new right. It merely confirmed the right acquired at the sale." *Boyd* v. *Longworth,* 11 Oh. 235, 252. The action of the Ohio court formally recognizing the equitable title and the rights petitioner had acquired at the sale thus gave petitioner nothing

it did not already have when bankruptcy intervened. Such action although occurring after bankruptcy intervened, is, as pointed out in the Petition (p. 13), no more than an exercise of jurisdiction "not inconsistent with the provisions of the Bankruptcy Act" which this court sanctions. *Callaway* v. *Benton,* 336 U. S. 132, 151. In view of § 67a(3) of the Bankruptcy Act, if the Ohio court had not confirmed the sale, it would seem that petitioner in the enforcement of its property rights would be entitled to have the Bankruptcy Court enter an order permitting the Ohio court to proceed with the matter of confirmation and enter an appropriate order as was done in *Jelks* v. *Aetna Life Ins. Co.* (C. A. 10) 134 F. (2d) 870. That case involved a judicial sale governed by Oklahoma law, which is like that of Ohio, the purchaser at a judicial sale obtaining an equitable title even before confirmation.

In attempting to distinguish *Jelks* v. *Aetna Life Ins. Co., supra,* Respondents have distinguished away their own case. Although in the *Jelks* case at the time the proceedings under § 75 of the Bankruptcy Act were begun the debtor under state law had no equity of redemption in the property sold at the judicial sale, nevertheless, the sale had not been confirmed when the bankruptcy proceedings were started. In that case the bankruptcy court granted the state court permission to proceed with the confirmation and then after the state court confirmed the sale, dismissed the bankruptcy proceeding. On appeal the Court of Appeals sustained this action, pointing out with respect to the lack of confirmation when bankruptcy was started, that under Oklahoma law by virtue of the sale "the equitable title passes to the purchaser; and the confirmation relates back to the date of the sale." In the instant case, as has been shown, there is, under Ohio law, no right of redemption from a judicial sale of personal property and, the Ohio law as to the title acquired by the

purchaser at a judicial sale is like that of Oklahoma. Yet Respondents concede that the *Jelks* case "does not in any way infringe" upon the rules as to the paramount and exclusive nature of bankruptcy jurisdiction upon which they rely.

These questions as to the effect of the rules as to the paramount and exclusive character of bankruptcy jurisdiction and the power of the Ohio court to confirm its judicial sale, after bankruptcy had intervened, as to none of which there is any direct authority, are of basic importance in the administration of the Bankruptcy Act and warrant review by this court.

Conclusion.

For the reasons set forth in the Petition and this Reply, it is respectfully submitted that the petition of Lafayette Steel Co., Inc., for a writ of certiorari should be granted.

Respectfully submitted,

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AMENDMENT TO PETITION FOR WRIT OF CERTIORARI.

In accordance with the notice of its intention to amend the petition in this case given Respondents by letter of January 9, 1951, Petitioner amends its petition in the following respects:

1. To be inserted after the word "confirmed" in the sixth line on page 9 of the Petition for a Writ of Certiorari:

> and when the sale is confirmed and a conveyance executed, these relate back to the date of sale, vesting legal title also in the purchaser as of that date.

2. To be inserted after the first full paragraph on page 13 of the Petition for a Writ of Certiorari:

> In the analogous situation of an agricultural composition or extension proceeding under Section 75 of the Bankruptcy Act begun after a judicial sale of property of the debtor, it has been held that state law is determinative of the effect of the judicial sale, *State Bank of Hardinsburg* v. *Brown,* 317 U. S. 135. And in such a case where the state law, like that of Ohio, is that the purchaser by reason of the judicial sale becomes the equitable owner of the property sold even before the sale is confirmed, it is held that the Bankruptcy Court acquires no jurisdiction over the property sold at a judicial sale held before but not confirmed until after the Section 75 proceedings were begun. *Jelks* v. *Aetna Life Ins. Co.* (C. A. 10), 134 F. (2d) 870.